

This record is a partial extract of the original cable. The full text of the original cable is not available.

130807Z Jan 05

C O N F I D E N T I A L SECTION 01 OF 02 RANGOON 000058

SIPDIS

STATE FOR EAP/BCLTV, EB  
COMMERCE FOR ITA JEAN KELLY  
TREASURY FOR OASIA  
USPACOM FOR FPA

E.O. 12958: DECL: 01/12/2015

TAGS: [EFIN](#) [ECON](#) [PGOV](#) [BM](#)

SUBJECT: BURMA: VICIOUS CYCLE OF ECONOMIC DESPONDENCY

REF: 04 RANGOON 542 AND PREVIOUS

Classified By: COM Carmen Martinez for Reasons 1.4 (B,D)

11. (C) Summary: One year after the GOB allowed most private banks to resume operations, the banking situation has improved little. Stringent regulations cap deposits at unreasonably low levels, Burma's chilly economic situation has dried up demand for loans, and the GOB still refuses to implement thoughtful banking reform. With banks so weak, and the GOB continuing to mismanage economic policy, a second crisis for the banks is possible. End summary.

Deposits are Too High

12. (SBU) The GOB allowed most private banks to resume taking deposits in February 2004 -- a year after closing due to a massive bank run (reftels). Before re-opening the banks, the GOB imposed several stringent new restrictions aimed at preventing future "irresponsible behavior" by bankers, but avoided necessary reforms. For example, bank lending and deposit rates are still capped below the rate of inflation and private banks still cannot handle foreign exchange. As expected, the impact on Burma's economy has been negligible. Three of the four largest pre-crash private banks remain shuttered (two, Asia Wealth and Myanmar Mayflower, suspected of money laundering and under investigation) and other banks are suffering under the new regulations combined with a very chilly business climate.

13. (C) According to the new regulations, banks may not have total deposits larger than seven times paid-in capital. Though confidence in the banking sector is not high, deposits have been good over the last year. Most of the private banks are quite small and long-ago exceeded the 7:1 ratio. One private banker said his bank was already at a deposit-capital ratio of 14:1 and a colleague's bank was at 28:1. The larger active private banks have kept their deposit ratio at 7:1 by periodically refusing to accept deposits from new customers. The GOB is taking notice of this cap busting. At the end of December 2004, the GOB's Bank Management Committee (chaired by a SPDC member with no economic experience) began once again to call in all private bankers for nightly reviews of the day's activities and "necessary instructions" for getting in line with the regulations. These all-hands nightly sessions had not occurred since March 2004.

Loans are Too Low

14. (SBU) The deposit problem is exacerbated, bankers tell us, by the low volume of new loans. After the banking crisis of 2003, the GOB forced private banks to call in all of their outstanding loans (performing or not). These borrowers have not returned since lending was re-commenced in mid-2004.

15. (C) This is the result of two factors. First and foremost, business confidence is at an all time low. On top of chronic economic mismanagement, over the last two years private business have faced several acute problems: a banking collapse, new U.S. economic sanctions, a freeze on agricultural exports, a hike in the cost of importing, and the purge of Prime Minister Khin Nyunt and his economically active military intelligence apparatus. Domestic investment is nearly zero as most businesses refuse to make any new deals until the future is clearer. Businesspeople tell us they are waiting for signals from the top and are reluctant to make any move that could later come back to haunt them. Even GOB projects started during Khin Nyunt's era have been halted awaiting explicit approval to continue. None has come. Businesses are expatriating their money or sticking it in banks or in the rice barrel hoping for better times.

16. (SBU) A second factor is the regulatory environment. Though loans are cheap (a maximum 15 percent interest rate with inflation in 2004 running about 20 percent), banks can only lend out 35 percent of the "forced-sale" value of a borrower's collateral. Furthermore, businesspeople report that as loans above 30 million kyat (about \$33,000) require special reporting to the GOB, few banks or borrowers want to

conduct such a deal and draw the attention of the authorities. Even if the loans flowed again, however, regulations prohibit total loans of more than 70 percent of total deposits (or roughly five times paid-in capital). Thus the volume of lending from the small banks allowed to operate will do little to spur the economy as a whole.

Comment: A Vicious Cycle Toward Collapse?

17. (C) A flourishing private banking sector is essential for sustainable economic growth in Burma. However, economic growth is dependent on a vibrant banking system. In this bad business climate with banks so poorly regulated, a vicious cycle has emerged. The economy is cold so businesses are reluctant to borrow and invest. Banks are not lending so they face difficulties staying profitable with the influx of deposits. Without new lending the economy will have trouble reviving. The GOB authorities do not understand the problem or are ignoring it. While authorities are apparently keen to enforce their draconian regulations, they show no signs of rationalizing the industry or freeing up or restructuring the largest private banks. All this points to a potential second private banking crisis as bank owners and investors lose money while being forced by the GOB to raise additional paid-in capital (by buying GOB bonds paying 9.5 percent) or turn away customers. End comment.  
Martinez